Lornex

MINING CORPORATION LTD.

ANNUAL REPORT 1972

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OFFICERS	Honorary Chairman - E. H. LORNTZSEN
	Chairman of the Board - R. W. WRIGHT, CBE
	President and Chief Executive Officer - R. D. ARMSTRONG
	Vice-President - G. R. ALBINO
	Vice-President - C. W. RENO
	Treasurer - J. VAN NETTEN
	Secretary - C. W. M. BURGE
DIRECTORS	G. R. ALBINO, Port Credit, Ont. W. A. ARBUCKLE, Montreal R. D. ARMSTRONG, Toronto E. B. GILLANDERS, Surrey, B.C. F. GREGORY, London, England R. HAMMOND-CHAMBERS, Edinburgh, Scotland J. H. HOUGH, Toronto N. B. IVORY, Montreal K. KAWAKAMI, Tokyo, Japan E. H. LORNTZSEN, Vancouver A. F. LOWELL, Toronto J. A. SADLER, Toronto R. W. WRIGHT, CBE, London, England
HEAD OFFICE	580 Granville St. - Vancouver
MINE OFFICE	P.O. Box 1500 - Logan Lake
PRINCIPAL BANKERS	Canadian Imperial Bank of Commerce - Vancouver and Toronto The Toronto-Dominion Bank - Toronto Bank of Montreal - Toronto
SOLICITORS	Clark, Wilson & Company - Vancouver Fasken & Calvin - Toronto
AUDITORS	Coopers & Lybrand - Vancouver
REGISTRAR AND TRANSFER AGENT	National Trust Company, Limited - Vancouver
SHARES LISTED	Vancouver Stock Exchange
THE ANNUAL GENERAL AND EXTRAORDINARY GENERAL MEETING	11.00 a.m., Tuesday, April 17, 1973 Bayshore Inn, Vancouver, British Columbia.

DIRECTORS' REPORT TO THE SHAREHOLDERS

Your Directors are pleased to submit this report on the affairs of the Company for the year ended December 31, 1972.

The year 1972 was of particular significance since it marked the completion of the development and construction of the Company's copper-molybdenum mine in the Highland Valley of British Columbia and the commencement of operations on October 1, 1972.

Net capital cost to December 31, 1972 was $142.7 million and operations for the three months ended on that date resulted in a net loss of $1,215,000.

Development and Construction

Completion of development and construction and the commencement of operations had been scheduled for the second quarter of 1972. Unexpected delays were encountered in completion of construction and, as a consequence, the first ore was not processed until April. Progress toward reaching the mill design average rate of 38,000 tons per day was delayed by mechanical difficulties normal in the early stages of a project of this scale. In addition operations were interrupted by a work stoppage over the period July 3 to August 9.

Mine development was carried out by the Company's forces with the equipment which is being used in mining operations.

During the development period a total of 60.9 million tons of overburden, waste rock and oxide ore was removed on schedule and within budget at rates that exceeded 150,000 tons per day at the peak of the pit preparation period. In addition 3.4 million tons of ore was mined during this period.

Design and construction of the process and ancillary facilities and of the townsite at Logan Lake was carried out by contractors under the direction of the Company. At the peak of construction activity the employment level reached 2,034.

As of this date the Logan Lake townsite development has been essentially completed to the stage currently planned. This comprises 185 houses, 46 townhouse units and 39 lots for mobile homes. The housing units are being made available to employees and others under purchase arrangements which have proven to be sufficiently attractive that virtually all of the available units have been either purchased or reserved for purchase. Additional construction may be undertaken if the need arises.

The village of Logan Lake is now a viable incorporated community readily accessible to larger communities, and offering to its some 900 residents a wide variety of physical and social amenities. All commercial services are provided by independent local businesses.

Operations

From the first introduction of ore to one mill line in April to September 30, 1972, during which period there was a work stoppage of some 37 days, a total of 2.7 million tons of ore was milled at an average mill head grade of 0.423% copper and an average recovery of 87.4%. Daily milling rates fluctuated during this period due to mill stoppages caused by mechanical problems and to

variations in hourly milling rates that occurred during the process of identifying and controlling the ore blend and ball charge combinations required to optimize the primary autogenous milling system employed by the Company.

During the three month operating period from October 1 to December 31, 1972, the milling and metallurgical data were:

	Total	December	November	October
Average daily milling rate (short tons)	30,998	34,537	33,807	24,741
Copper mill head grade	0.429%	0.408%	0.439%	0.447%
Recovery	87.9%	88.2%	87.3%	88.3%

It should be noted that grades and recoveries normally fluctuate during an initial operating period and the foregoing metallurgical data should not be regarded as representative.

A total of 2.9 million tons of ore was milled during this period from which approximately 20.9 million payable pounds of copper, 581,000 payable pounds of molybdenum and 80,000 payable ounces of silver were recovered.

Milling rates in excess of the design average rate of 38,000 tons per day are now being achieved for sufficiently extended periods to support the opinion expressed earlier that the design rate will be consistently exceeded in due course.

The operating profit for the three month period was $1,534,000 after providing for amortization and depreciation of $1,781,000. After providing for interest charges of $2,749,000 the net loss for the period was $1,215,000.

Financial

The Company's capital financing was completed during the year; this involved drawing down the residual amount of $24 million available under the Bank Loan Agreement. In addition, Rio Algom Mines Limited purchased Units of Income Debentures and shares for $4,352,000 during 1972 under the supplementary financing provisions of a Construction and Management Agreement. Under a previous agreement 27.5% of these Units were sold at cost by Rio Algom to The Yukon Consolidated Gold Corporation Limited.

Sales Agreements

As previously reported, the entire copper concentrate production of the Lornex mine has been contracted for by a group of Japanese smelting companies for a period of twelve years; the projected annual output of molybdenum concentrates estimated at about 3 million pounds per year of contained molybdenum has been contracted for by a United States company for a period of five years.

In February 1972, the Company received a formal request from the Japanese purchasers for a revision of certain terms of the Lornex copper concentrate sales contract. On March 28, 1972 the Canadian Federal Government asked that all Canadian producers refrain, until April 30, 1972, from making any amendments to established legal obligations in order to allow the Canadian government to make a careful study of the circumstances involved with Japanese purchasers. The Company complied and, having been subsequently released from such request, resumed negotiations with the Japanese purchasers on May 23, 1972. After a series of meetings an agreement was reached that is considered to accord appropriate recognition to the interests of the parties concerned.

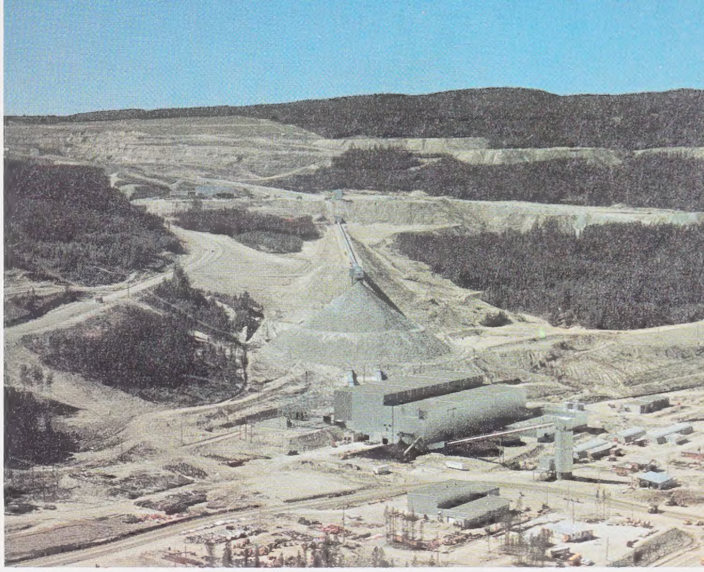
1. *Lornex, the copper-molybdenum mine in British Columbia's Highland Valley, began production in 1972. Overall view shows the plant and related facilities in foreground, the coarse ore stockpile and conveyor from the primary crusher, and in the upper left, the production pit.*

2. *Logan Lake, the community built to house Lornex personnel and their families, was virtually completed in 1972. Like its larger counterparts, it even has townhouses, the latest fashion in urban living.*

3. *Lornex: A bolt is tightened on a giant autogenous mill just prior to start of production.*

4. *First shipment of copper concentrate on its way to Ashcroft from where it was trans-shipped by rail to Vancouver.*

1.



2.

4.

3.

During the year there were three shipments containing in total 35.3 million payable pounds of copper in concentrate.

Environment

The Company has been acutely conscious of environmental considerations and all possible actions have been taken to prevent pollution of the environment by the Lornex mine complex and the village of Logan Lake. Prior to commencement of operations an ecological inventory was carried out which included a count of the wild animal life and recording of existing vegetation and fish life. A chemical analysis of streams in the area was also made to establish pollution levels and background metal content. These studies made by independent consultants will provide an authoritative record of the environment of the locality prior to the start of operations and will establish a base from which to measure any changes resulting from mining activity.

The tailings system has been constructed and is being operated in accordance with the pollution control permit issued by the British Columbia Pollution Control Board. The two tailings dams have been constructed of selected material including clay cores to prevent seepage and the tailings system includes wells and pumps near each dam to monitor underground water for any potential contamination.

During operations the appearance of the mine complex will be orderly; drainage will be controlled and directed to a basin where suspended solids will be permitted to settle out before the clear water is decanted into the natural drainage system. Suitable vegetation will be planted on waste dumps and tailings areas that become inactive.

Employee Relations

The collective agreement between the Company and the United Steelworkers of America expired on June 30, 1972. Negotiations had been in progress since late 1971, but a new agreement had not been reached by the expiry date and the project was shut down by a strike on July 3. Work was resumed on August 9 after an agreement was signed with effect from August 7, 1972 until June 30, 1974. Except for this work stoppage, employee relations have been good.

Management

On December 15, 1972, Mr. Charles W. Reno, formerly Operations Manager, was appointed a Vice-President and General Manager of the Company in succession to Mr. Norman F. Warren. Mr. Warren's contribution in bringing the Lornex mine into production is acknowledged with gratitude.

Appreciation

The Directors of the Company recognize that completion of the development and construction work on this very large project and commencement of operations in 1972 was a demanding task. They wish to acknowledge the confidence and support of the Company's shareholders and to record their appreciation for the competent and diligent efforts of the many companies and individuals that were involved in this achievement.

On behalf of the Board,

Vancouver, B.C.,
February 23, 1973.

R. D. ARMSTRONG,
President.

Auditors' Report

To the Shareholders of
Lornex Mining Corporation Ltd.:

We have examined the statement of financial position of Lornex Mining Corporation Ltd. as at December 31, 1972, and the statements of earnings and deficit, exploration, development and construction expenditures and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these financial statements present fairly the financial position of the Company as at December 31, 1972 and the results of its operations and the changes in its financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Vancouver, British Columbia.
February 8, 1973.

COOPERS & LYBRAND
Chartered Accountants.

ACCOUNTING POLICIES

The principal accounting policies followed by Lornex Mining Corporation Ltd. are summarized hereunder:

REVENUE FROM MINE PRODUCTION AND VALUATION OF CONCENTRATES AWAITING SHIPMENT

A group of Japanese smelting companies has contracted to purchase the Company's entire production of copper concentrate for a period of twelve years. A United States company has contracted to purchase the projected annual molybdenum concentrate production for a period of five years.

Production is valued and taken into income as revenue from mine production at estimated realizable metal prices less provision for possible fluctuation in price; concentrates awaiting shipment are also valued on this basis. Adjustments are made to revenue from mine production with respect to concentrate shipments when the actual metal price is known and the final weight and assay adjustments are determined. Estimated smelting, refining and marketing charges are accrued at time of production and these charges are also adjusted with respect to shipments when the final weight and assay adjustments and marketing charges are determined.

At December 31, 1972 inventories of 4,460,000 payable lbs. of copper and 654,000 payable lbs. of molybdenum contained in concentrates awaiting shipment were valued as described above; the final price had been established in respect of a shipment of approximately 13.4 million payable pounds of copper for which final weight and assay adjustments and marketing charges had not been determined.

CONVERSION OF UNITED STATES CURRENCY

The accounts in United States currency are stated in Canadian dollars on the following basis:

Current assets and current liabilities at year-end exchange rates; all other assets and long term liabilities at rates in effect at time of transactions, and revenues and expenses at actual rates prevailing during the year.

MINE SUPPLIES

Mine supplies are valued at average cost.

DEPRECIATION AND AMORTIZATION

Depreciation is provided on mining equipment on a straight-line basis over the shorter of its physical life or the estimated life of the mine. The cost of plant and equipment, mining properties and preproduction expenditures is amortized on a unit-of-production basis over the estimated life of the mine.

Statement of Financial Position

DECEMBER 31, 1972

($000's omitted)

	1972	1971
CURRENT ASSETS:		
Cash and short term deposits	$ 5,253	$ 4,362
Accounts and settlements receivable and prepaid expenses	2,816	608
Concentrates awaiting shipment	2,844	—
Mine supplies	4,337	—
Total	15,250	4,970
Less:		
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	1,948	1,884
Payable to Rio Algom Mines Limited	3,245	1,351
Accrued interest on bank loans and 8¾% Notes	1,803	103
Long term debt due within one year (note 4)	6,153	—
Total	13,149	3,338
WORKING CAPITAL	2,101	1,632
Plant and equipment, less depreciation (note 2)	93,962	11,430
Construction in progress	—	72,499
Mining properties and preproduction expenditures less amortization (note 3)	46,925	31,698
	140,887	115,627
TOTAL ASSETS LESS CURRENT LIABILITIES	142,988	117,259
Deduct:		
Long term debt (note 4)	133,147	106,558
EXCESS OF ASSETS OVER LIABILITIES	$ 9,841	$ 10,701
OWNERSHIP EVIDENCED BY (note 5):		
Capital stock		
Authorized —		
9,500,000 common shares, par value of $1.00 each		
4,500,000 Class A shares, par value of $1.00 each		
Issued —		
7,331,904 common shares (7,138,584 shares in 1971)	$ 7,332	$ 7,139
867,758 Class A shares (712,018 shares in 1971)	868	712
	8,200	7,851
Premium less discount on shares issued for cash (includes $6 premium on shares issued under stock option plan in 1972)	2,856	2,850
Deficit	(1,215)	—
Total	$ 9,841	$ 10,701

Approved on behalf of the Board:

NEIL B. IVORY, Director. R. D. ARMSTRONG, Director.

Statement of Earnings and Deficit
YEAR ENDED DECEMBER 31, 1972
($000's omitted)

Revenue from mine production	$ 10,636	
Less smelting, refining and marketing charges	1,689	
Net revenue		$ 8,947
Expenses:		
Operating expenses	5,632	
Amortization and depreciation	1,781	7,413
Operating profit		1,534
Interest on long term debt		2,749
Net loss for the year and deficit at December 31, 1972		$ (1,215)
Net loss per share of capital stock (note 5)		(15¢)

The above statement of earnings reflects only the three months from commencement of operations on October 1, 1972 to December 31, 1972.

Statement of Exploration, Development and Construction Expenditures

YEAR ENDED DECEMBER 31, 1972

($000's omitted)

	Balance Dec. 31, 1971	Expenditures during year	Balance Dec. 31, 1972
Preliminary exploration and project investigation	$ 7,400	$ —	$ 7,400
Equipment	21,798	3,686	25,484
Mine development and plant construction in progress	71,919	16,405	88,324
Townsite development	5,809	1,929	7,738
Interest and financing charges	3,600	3,764	7,364
Expenditures involving outlay of funds	110,526	25,784	136,310
Other charges and (credits):			
Accrued interest on income debentures and loans from associated companies	3,711	2,871	6,582
Value ascribed to share capital (note 4)	3,330	348	3,678
Sale of townsite property	(1,940)	(1,962)	(3,902)
Net Capital Cost	$ 115,627	$ 27,041	$ 142,668
Allocated to:			
Plant and equipment (note 2)	$ 11,430	$ 83,823	$ 95,253
Construction in progress (see note)	72,499	(72,499)	—
Mining properties (note 3)	1,530	(475)	1,055
Preproduction expenditures (note 3)	30,168	16,192	46,360
	$ 115,627	$ 27,041	$ 142,668

NOTE:

On completion of the construction program on October 1, 1972 expenditures on construction in progress were allocated to plant and equipment, mining properties and preproduction expenditures; certain expenditures were also re-allocated between these classifications.

Statement of Changes in Financial Position

YEAR ENDED DECEMBER 31, 1972

($000's omitted)

		1972	1971
SOURCE OF FUNDS:			
Operations			
Net loss for year		$ (1,215)	$ —
Add charges against earnings not involving current outlay of funds:			
Amortization and depreciation		1,781	—
Interest on Income Debentures, etc.		1,111	—
Total funds from operations		1,677	—
Bank loans		24,000	36,000
Units of 8½% Series A Income Debentures and shares		4,352	16,141
Units of 8¾% Notes and shares		—	16,636
Housing loans (net)		407	270
Issue of common shares under stock option plan		7	—
		30,443	69,047
DISPOSITION OF FUNDS:			
Expenditures on exploration, development and construction		27,041	81,506
Reduction of long term debt (amounts due within one year)			
Bank loans	$ 5,900		
8¾% Notes	253	6,153	—
		33,194	81,506
Less charges not involving current outlay of funds:			
Value ascribed to share capital (note 4)		348	1,385
Interest accrued prior to October 1, 1972 on Income Debentures and loans from associated companies		2,872	2,719
		3,220	4,104
		29,974	77,402
INCREASE OR (DECREASE) IN WORKING CAPITAL		$ 469	$ (8,355)

Notes to the Financial Statements

YEAR ENDED DECEMBER 31, 1972

1. ACCOUNTING POLICIES

The information on page 8 presents a summary of certain accounting policies and is an integral part of these financial statements.

2. PLANT AND EQUIPMENT

	1972	*1971*
Plant and equipment at cost	$98,419,798	*$13,010,970*
Less accumulated depreciation at October 1, 1972 included in preproduction expenditures shown in note 3 below	3,167,054	*1,581,271*
	95,252,744	*11,429,699*
Less accumulated depreciation included in statement of earnings and deficit	1,291,092	—
	$93,961,652	*$11,429,699*

3. MINING PROPERTIES AND PREPRODUCTION EXPENDITURES

	1972	*1971*
Mining properties, at cost	$ 1,055,009	*$ 1,529,915*
Less accumulated amortization	10,871	—
	1,044,138	*1,529,915*
Preproduction expenditures at cost (including depreciation)	46,360,455	*30,168,480*
Less accumulated amortization	479,230	—
	45,881,225	*30,168,480*
	$46,925,363	*$31,698,395*

4. LONG TERM DEBT

	1972	*1971*
Bank loans (with interest and terms as stated hereunder)	$ 60,000,000	*$ 36,000,000*
Less portion included in current liabilities	5,900,000	—
Long term portion (including Can. $6,000,000 payable in U.S. dollars)	54,100,000	*36,000,000*
8¾% Notes due as stated hereunder ($26,500,000 U.S.)	26,836,406	*26,836,406*
Less portion included in current liabilities ($250,000 U.S.)	253,173	—
Long term portion ($26,250,000 U.S.)	26,583,233	*26,836,406*
8½% Series A Income Debentures due December 31, 1985	44,093,000	*39,741,000*
Housing loans	677,737	*269,973*
Accrued interest on income debentures	7,693,055	*3,710,780*
	$133,147,025	*$106,558,159*

Repayment of the bank loans is collaterally secured under a Trust Deed by the pledge of first mortgage bonds, secured by a first fixed and specific charge and a first floating charge on the assets of the Company. The interest rate on such loans is 1¼% above the minimum commercial lending rate adjustable from time to time by each bank independently; the December 31, 1972 rate was 7¼% per annum.

Repayment of the 8¾% Notes is collaterally secured under a Trust Deed by the pledge of second mortgage bonds, secured by a second fixed and specific charge and a second floating charge on the assets of the Company.

Repayment of the bank loans begins in the calendar quarter following the commencement of commercial production; as defined in the loan agreements this occurred on August 1, 1972. 75% of the Company's net operating profit as defined in the Bank Loan Agreement is to be applied to repayment of the principal of the loans for the first five calendar quarters of operations. Subsequently 90% of the Company's net operating profit is to be applied to the repayment of the loans until repaid in full and then to the repayment of the 8¾% Notes under the Japanese Financing Agreement. The cumulative minimum repayments of principal required to be made are as follows:

	Cumulative Minimum Repayments of Principal	
Due In	Bank Loans	8¾% Notes
1973	$ 5,900,000	$ 250,000 U.S.
1974	16,300,000	500,000 U.S.
1975	29,300,000	750,000 U.S.
1976	42,300,000	1,000,000 U.S.
1977	54,400,000	1,250,000 U.S.
1978	60,000,000	8,350,000 U.S.
1979	—	21,650,000 U.S.
1980	—	26,500,000 U.S.

The principal amount of the Income Debentures is to be repaid by way of annual sinking fund payments from all of the operating profits of the Company after all other forms of long term debt have been paid in full. The amounts and timing of the required sinking fund payments are defined in the Income Debenture Indenture and are dependent on the operating profits of the Company together with certain other factors. The sinking fund payments are to be used to redeem the Income Debentures at par.

The accrued interest of $7,693,055 at December 31, 1972 may not be paid until the required interest and principal repayments have been made and certain other conditions have been met under the terms of the Bank Loan Agreement and the Japanese Financing Agreement.

During the year the Company sold 4,352 Units under the supplementary financing provisions of a Construction and Management Agreement with Rio Algom Mines Limited at a price of $1,000 per Unit. Each Unit consisted of $1,000 principal amount of Income Debentures and 80 Class A shares. Accordingly the Company issued 348,160 fully paid Class A shares comprised in Units sold; a value of $348,160 has been ascribed to the Class A shares so issued, which amount is reflected in the statement of exploration, development and construction expenditures.

5. CAPITAL STOCK

	Common		Class A	
	Shares	Amount Paid Up	Shares	Amount Paid Up
Shares Issued:				
At December 31, 1971	7,138,584	$7,138,584	712,018	$ 712,018
Under Stock Option Plan	900	900	—	—
For provision of finance equal to the par value of $1 per share (note 4)	—	—	348,160	348,160
	7,139,484	7,139,484	1,060,178	1,060,178
Conversion of Class A to common shares	192,420	192,420	(192,420)	(192,420)
Balance, December 31, 1972	7,331,904	$7,331,904	867,758	$ 867,758

The Class A shares are non-voting, are not entitled to dividends, and may be converted to common shares at any time at the option of the holder on the basis of one common share for each Class A share.

At December 31, 1972, 1,727,418 common shares were reserved:

(a) 1,628,318 common shares for issue in exchange for the 867,758 Class A shares issued and outstanding and for the 760,560 Class A shares which may be issued under the terms of the Construction and Management Agreement;

(b) 99,100 common shares for issue under a Stock Option Plan. Options may be granted to employees of the Company and to certain employees of Rio Algom Mines Limited. Outstanding options have been granted to purchase 66,800 common shares at prices varying from $7.29 to $8.10 per share; these options expire on varying dates from September 27, 1976 to February 20, 1978.

In addition 760,560 Class A shares are reserved to satisfy obligations of the Company which may arise under the provisions of the Construction and Management Agreement with Rio Algom (note 6(a)).

Net loss per share has been calculated on the total number of shares outstanding at December 31, 1972, including both common and Class A shares.

The Trust Deeds and Indentures prohibit the payment of dividends until all loans and accrued interest have been paid in full.

6. COMMITMENTS AND CONTINGENT LIABILITIES

(a) Rio Algom Mines Limited has agreed to supervise and manage the business of the Company until December 1, 1984 and to incur and pay, on behalf of the Company, operating costs of the Company incurred prior to August 1, 1976. The Company has agreed to pay Rio Algom a management fee of $250,000 per annum.

If the Company is unable to reimburse Rio Algom for any of the aforementioned costs Rio Algom may elect to receive Units of the Company's Income Debentures and Class A shares instead of cash at a later date. The maximum number of such Units which could be issued is 9,507, comprised of $9,507,000 principal amount of Income Debentures and 760,560 Class A shares.

(b) The Company has a contingent liability to buy back 158 houses at the Logan Lake townsite for $3,823,490 until December 31, 1982.

7. REMUNERATION OF DIRECTORS AND SENIOR OFFICERS

During the year ended December 31, 1972 the aggregate direct remuneration paid or payable by the Company to the Directors and Senior Officers of the Company was $173,651.

Rio Algom

Rio Tinto

Printed in Canada.